



United States
General Accounting Office
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Office of the General Counsel

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November 18, 1998

The Honorable Alfonse M. D'Amato
Chairman
The Honorable Paul S. Sarbanes
Ranking Minority Member
Committee on Banking, Housing, and Urban Affairs
United States Senate

The Honorable Thomas J. Bliley, Jr.
Chairman
The Honorable John D. Dingell
Ranking Minority Member
Committee on Commerce
House of Representatives

Subject: Securities and Exchange Commission: OTC Derivatives Dealers

Pursuant to section 801(a)(2)(A) of title 5, United States Code, this is our report on a major rule promulgated by the Securities and Exchange Commission (SEC), entitled "OTC Derivatives Dealers" (RIN: 3235-AH16). We received the rule on October 26, 1998. It was published in the Federal Register as a final rule on November 3, 1998. 63 Fed. Reg. 59362.

The rule adopts the regulatory framework that allows U.S. securities firms to establish separately capitalized entities to conduct over-the-counter (OTC) derivatives business. The rule will permit these non-broker-dealer entities to deal in both security and non-security derivative instruments in competition with U.S. banks and off-shore firms. The SEC asserts that regulation is intended in part to improve the efficiency and competitiveness of U.S. securities firms that are active in global OTC derivatives markets.

Enclosed is our assessment of the SEC's compliance with the procedural steps required by section 801(a)(1)(B)(i) through (iv) of title 5 with respect to the rule. Our review indicates that the SEC complied with the applicable requirements.

If you have any questions about this report, please contact Alan Zuckerman, Assistant General Counsel, at (202) 512-4586. The official responsible for GAO evaluation work relating to the Securities and Exchange Commission is Thomas McCool, Director, Financial Institutions and Markets Issues. Mr. McCool can be reached at (202) 512-8678.

Robert P. Murphy
General Counsel

Enclosure

cc: The Honorable Jonathan G. Katz
The Secretary of the Securities and
Exchange Commission

ANALYSIS UNDER 5 U.S.C. § 801(a)(1)(B)(i)-(iv) OF A MAJOR RULE
ISSUED BY
THE SECURITIES AND EXCHANGE COMMISSION
ENTITLED
"OTC DERIVATIVES DEALERS"
(RIN: 3235-AH16)

(i) Cost-benefit analysis

Although the SEC was not required to prepare a cost-benefit analysis of the rule, it did prepare such an analysis based in large part on the information furnished by five securities firms. These organizations provided cost information on a confidential basis. In sum, the SEC states that most responding firms expected significant benefits because of the regulatory capital savings, increased capital efficiency, and efficiencies resulting from business consolidation, all of which outweighed the increased one-time and continuing operating costs associated with conducting the OTC derivatives business as OTC derivatives dealers.

(ii) Agency actions relevant to the Regulatory Flexibility Act, 5 U.S.C. §§ 603-605, 607, and 609

The Initial Regulatory Flexibility Analysis (IRFA) was incorporated in the notice of proposed rulemaking, 62 Fed. Reg. 67940, December 30, 1997. The SEC sought comments on the proposed rulemaking, including comments on the initial regulatory flexibility analysis.

The IRFA provides the information required by paragraphs 603(b)(1), (b)(2), (b)(3), and (b)(4). It describes the reasons for the proposed agency action; its objectives; the legal basis; and the reporting, recordkeeping, and other compliance requirements of the proposed rule.

The rule incorporates the Final Regulatory Flexibility Analysis (RFA) consistent with the requirements of 5 U.S.C. § 604. The analysis notes that no small entities are expected to be affected by the rule since the capitalization requirements for an OTC derivatives dealer will prevent a small entity from registering as an OTC derivatives dealer. The SEC satisfies the requirements of section 604(a). It describes the need for and objective of the final rule.

(iii) Agency actions relevant to sections 202-205 of the Unfunded Mandates Reform Act of 1995, 2 U.S.C. §§ 1532-1535

As an independent regulatory agency, the SEC is not subject to title II of the Unfunded Mandates Reform Act of 1995.

(iv) Other relevant information or requirements under acts and executive orders

Administrative Procedure Act, 5 U.S.C. §§ 551 *et seq.*

The SEC promulgated this rule under the notice and comment procedures of 5 U.S.C. § 553. A notice of proposed rulemaking was published on December 30, 1997, 62 Fed. Reg. 67940. The SEC received comments in response to the notice, and in its report indicates that it gave full consideration to the comments filed by the interested parties.

Paperwork Reduction Act, 44 U.S.C. §§ 3501-3520

The information collection requirements have been reviewed by the Office of Management and Budget (OMB) and has been assigned OMB control number 3235-0498.

Statutory authorization for the rule

Securities Exchange Act of 1934, 15 U.S.C. 78a *et seq.*

Executive Order No. 12866

As the rule is promulgated by an independent regulatory agency, it is not subject to the review requirements of E.O. 12866.